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SIPDIS

SENSITIVE
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AF/S FOR S. HILL
NSC FOR SENIOR AFRICA DIRECTOR B. PITTMAN
STATE PASS TO USAID FOR L.DOBBINS AND E.LOKEN
TREASURY FOR J. RALYEA AND T.RAND
COMMERCE FOR BECKY ERKUL
ADDIS ABABA FOR USAU
ADDIS ABABA FOR ACSS

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SUBJECT: NO END IN SIGHT TO ZIMBABWE'S ELECTRIC POWER WOES

Summary

¶1. (SBU) Electric power demand in Zimbabwe far outweighs Zimbabwe Electricity Supply Authority's (ZESA) capacity to supply, and low and erratic coal supplies from Hwange Colliery exacerbate the problem. The GOZ will not allow ZESA to raise its tariffs, among the lowest in the world, to a level that will recover the cost of production, transmission and distribution, plus provide for capital investment and repairs. Foreign currency shortages have pushed ZESA deeply into arrears with regional utilities, further reducing supply. Plagued in addition by vandalism and the loss of skilled staff, ZESA is pursuing stop gap measures to step up domestic power production, earn foreign currency, and secure power supplies from Mozambique for major exporters who can pay in foreign currency. In the meantime, rolling power outages cripple the rest of industry and frustrate consumers. Without a friendly business climate and substantial investment in additional capacity, there is no end in sight for Zimbabwe,s power woes. End Summary

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Acute Power Supply/Demand Mismatch

¶2. (SBU) ZESA CEO Benjamin Rafemoyo told us that demand for electricity in Zimbabwe is about 1,850 MW in summer, rising to 2,200 MW in winter or to 2,800 MW when including suppressed demand. Although Zimbabwe,s power demand is declining as the economy shrinks, it still ranks second in the region after South Africa. On the supply side, even if all of Zimbabwe's power plants operated at full capacity,

Zimbabwe would still have a power shortfall ranging between 25 and 57 percent of demand.

¶3. (SBU) Zimbabwe has five electric power plants: the Hwange thermal power plant with installed capacity of 780 MW, the Kariba South hydroelectric plant with 750 MW capacity, and three smaller coal-powered thermal plants in Harare, Bulawayo and Munyati with a combined capacity of 170 MW. While the total installed capacity of the five plants is 1,700 MW, actual generation fell to less than half that amount--830 MW--in October. Historically, the demand/supply gap was easily filled by power imports from SNEL (Societe Nationale d'Electricite) in the DRC, Eskom in South Africa and HCB (Hydroelectrica de Cahora Bassa) in Mozambique. However, supply from the region has dropped to a trickle due primarily to South Africa,s own supply/demand mismatch and ZESA,s hard currency arrears to regional utilities.

Crumbling Infrastructure

¶4. (SBU) In a meeting with econoff on October 16, Rafemoyo said there had been no significant investment in Zimbabwe's electric power industry since the late 1990s and the average age of power plant equipment was 45-50 years. Obsolete equipment was being "patched up" to prolong its life and the Hwange power plant had been producing only about 100 MW of its 780 MW capacity in October, primarily due to lack of coal. Hwange Colliery, like the power plant it supplies two kilometers away, is vexed with old and unreliable equipment, resulting in low and erratic supplies of coal. In recent months, for example, the mine,s dragline excavator had been

out of commission for three weeks, its primary and secondary crushers had failed for days, and the conveyor system to the power plant had suffered a 1 1/2 km long tear.

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The Supply Backbone) Low-Cost Hydroelectric Power
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¶5. (U) Rafemoyo said the backbone of the domestic power industry had shifted in recent years from Hwange to the low-priced and reliable power of the Kariba hydroelectric plant on the Zambezi river on Zimbabwe's northern border. Zimbabwe's Kariba South plant is operating at close to 98 percent capacity and producing 730 MW. It is, of course, highly dependent on Lake Kariba,s water level; the waters rose this past year but not enough to run Kariba South,s six generators at full throttle.

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No Output from the Harare, Bulawayo or Munyati Plants
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¶6. (SBU) Diminished and erratic coal output from Hwange Colliery has also contributed to the effective shutdown of Zimbabwe,s three thermal power stations at Munyati, Bulawayo and Harare. Paul Markham, Rio Zim,s technical director, told econ specialist on October 22 that the three plants were designed for higher calorific-value beneficiated coal from Hwange Colliery which was now unavailable. Consequently, none of the three small plants had produced any power for months, although they continued to carry the overhead cost of a full labor force. Even if the coal were available, National Railways of Zimbabwe (NRZ) did not have reliable locomotives, wagons and signaling equipment to transport it to the power plants in a cost effective manner, according to Markham.

Uneconomic Tariffs) ZESA's Albatross

¶7. (SBU) The GOZ has not allowed ZESA to raise tariffs to a

cost-recovery level; consequently Zimbabwe's electric bills are among the cheapest in the world. Learnmore Nechitoro, economist at the Zimbabwe Electricity Regulatory Commission (ZERC), related to econoff on October 24 that ZESA had sought a 560 percent tariff increase in early 2006 and received ZERC and Cabinet approval, only to have Reserve Bank of Zimbabwe (RBZ) Governor Gono intercede and block the increase on the grounds that it would be inflationary. Cabinet eventually approved the increase but spread out over a year. ZABG bank senior economist David Mupamhadzi commented to us on October 30 that hyperinflation would inevitably erode modest incremental increases in tariffs, as happened last year, and the public utility needed a large price hike.

¶8. (SBU) Nechitoro pointed out that electricity made up an average of only 12-15 percent of total production cost across industries; cost-recovery tariffs therefore would not increase prices commensurately. He said the current blended tariff of about Z$1,300/kwh (tariffs range from about Z$380/kwh for Kariba's power to Z$18,000/kwh for the Harare plant) covered only about one-fifth or one-sixth of the cost of power generation, transmission and distribution. Appearing before the Parliamentary Portfolio Committee on Mines, Environment and Tourism on October 18, ZERC

Commissioner General and Chairperson Dr. Mavis Chidzonga called for a 316 percent increase in ZESA's tariffs, but Nechitoro remarked that the figure was two months old and already overtaken by inflation.

¶9. (SBU) In discussing Zimbabwe's unviable electricity tariffs, Alison Chikova, Chief Engineer at Southern African Power Pool (SAPP) in Harare pointed out to us on October 17 that ZESA,s rate of return in the period April 2006 to March 2007 was negative 48 percent and its net income was negative US$ 1.77 billion. He emphasized the need for competitive tariffs in Zimbabwe. Rafemoyo acknowledged that Zimbabwe needed private investors, especially in greenfield projects, and pointed out that the Electricity Amendment Act Number 3 of 2003 provided for the establishment of independent power producers (IPP), but the return to investors as measured by tariffs had to be attractive.

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Woes from Arrears to Vandalism, Brain Drain, Tight Terms
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¶10. (SBU) Rafemoyo said ZESA was no longer importing power from Eskom (as recently as June it was importing 50 MW) and it was netting off its debt with fees for the transmission of HCB power from Mozambique to South Africa. ZESA's remaining debt to Eskom was inconsequential (less than US$1,000). Zambia did not export power to Zimbabwe. SNEL supplied about 50 MW (down from 100 in June) to Zimbabwe, but vandalism and other problems along the very long transmission line made for erratic supply. As of October 16, ZESA was US$1.5 million in arrears to SNEL, according to Rafemoyo.

¶11. (SBU) HCB is Zimbabwe's most dependable foreign supplier. The company has a contractual obligation to supply 50 MW but could supply as much as 300 MW. Rafemoyo said ZESA was under intense pressure to pay the government of Portugal about US$29 million in ring-fenced arrears prior to year end when Portugal transfers 85 percent of its ownership of HCB to the government of Mozambique. Several days after our discussion with Rafemoyo, the press reported that ZESA had made a payment of US$20 million to HCB. Nechitoro explained that recent trends in regional power agreements toward shorter terms (6-12 months, as opposed to about 3 years), higher prices, and non-firm rather than firm supply commitments adversely affected Zimbabwe's ability to tap into regional power.

¶12. (SBU) ZESA is also increasingly plagued by theft of its power lines for copper and of oil from transformers.

Nechitoro lamented that scarce resources earmarked for expansion projects were being channeled more frequently to replacing vandalized equipment. Furthermore, Rafemoyo admitted that ZESA was hard put to retain its engineers and skilled labor force under poor working conditions and low salaries. He jested that ZESA's invoices were as ridiculous as its pay slips.

¶13. (SBU) As a result of power shortfalls and breakdowns, for the past half year Zimbabwe has been suffering rolling power outages that have gone well beyond ZESA's announced load shedding schedule. The outages have reduced industrial production, especially in the mining sector, constrained retail trade and had a devastating effect on the production of irrigated winter wheat. Andrew Ferreira, president of the Zimbabwe Tobacco Association, told us on October 30 that

growers of irrigated tobacco, which went into the ground on September 1, were struggling to water their crop under unpredictable power supplies.

Looking Ahead) ZESA Pins Its Hopes(.

¶14. (U) Rafemoyo recounted with particular pride the electricity purchasing agreement that ZESA entered into with NamPower in April 2007. The Namibian utility is funding the sequential refurbishment of four of Hwange's six units which will increase Hwange's capacity by 400 MW by October 2008. Beginning in January 2008, when the first refurbished unit is scheduled to go back on line, NamPower will draw guaranteed 50 MW from the plant, rising to 150 MW over a five year period.

¶15. (U) The ZESA CEO said that an agreement reached between ZESA and the Chamber of Mines in September would unlock an additional 200 MW from HCB. It allowed large mining companies to pay for power with their export earnings in exchange for uninterrupted power supply. Implemented on October 1, 2007, he said the deal would also provide some surplus power to the grid by late October.

¶16. (SBU) ZERC has approved four IPPs, none of which, however, contributes significantly to the national grid. ZESA is seeking investment partners - to date without success - for the expansion of Kariba South by 300 MW; for a major hydroelectric power plant in the Zambezi's Batoka gorge (vigorously opposed by conservationists and the local tourist industry); for expansion of the Hwange plant by 600 MW; and for development of coal-bed methane in Lupane (Matebele North province). Rio Zim is in discussions with investors about construction of the long envisioned 2000 MW Gokwe North power plant in Midlands, to be supplied by its Sengwa coal mine. Rio Zim's Markham told us the cost (nearly US$5 billion including improvements to the mine) had more than doubled since the project was first mooted in 1997.

¶17. (SBU) ZESA Enterprises has a supply-credit arrangement with China in which loans are secured by contract-grown tobacco. Rafemoyo said the deal had yielded less foreign exchange than anticipated (US$3.5-4 million this year, US$8 million in 2006 and US$10 million in 2005), but had helped ZESA secure equipment and service debt.

Comment

¶18. (SBU) Without viable tariffs, secure property rights, and substantial investment in additional capacity, no combination of stop gap measures will put an end to the rolling power outages that are vexing consumers and industry alike and sending broad swathes of residential and industrial Harare ever more frequently into darkness. Allowing major

exporters to pay for power imports in foreign currency is a first step toward acknowledging the need for viable tariffs, but it is a typically piecemeal approach to economic reform. As competition with South Africa for power in the regional market quickens, the prospects for meeting Zimbabwe's power needs under the present economic policies are dimming, along with the lights.
DHANANI